



CELEBRATING  
65 YEARS

# nareb

## Short-term thinking and long-term investing

May 12, 2010 - Appraisal & Consulting

In real estate, the decision to make repairs to short-lived items can be supported by an analysis of cost versus benefit. Yet, when the issue is structural integrity the problem lies within the long-lived components and any expenditure incurred to cover up such a problem with superficial repairs is likely to be wasted. On the slight chance that the cover-up is temporarily effective, the building could ultimately collapse causing greater harm and loss.

Public policy and real estate value are intertwined, most noticeably in the current climate, within the financial sector. The political argument and strategy of the day seems to be that we should not do anything that is immediately painful, even though it will ultimately provide greater and long-lasting economic benefits. In other words, think of the short-term and take the easy way out. Too often, it seems that the easy way is to throw money at short-term superficial fixes and kick the can down the road. Yet, to anyone making an analysis of the risk profile of the asset (real estate or a nation), the problem was not cured. So then, what happens to the value of the whole?

The nation's risk profile may be reflected by the continued decline in the value of the dollar for which I see no immediate end in sight. High unemployment and excess manufacturing capacity, both of which we are currently experiencing, act in opposition to inflation. Also, as witnessed by the Federal Reserve's recent decision not to increase interest rates with the hopes of encouraging the nascent economic recovery, there is apparently sufficient evidence that such an increase is not yet needed to prevent inflation. The bigger question is: as a result of our spending pattern how long will it be before external pressures, rather than fear of inflation, force a substantial increase in rates?

Affordability, expressed in the simplest terms as the amount of a monthly payment, has a direct effect on single family home values. Given the past ten years' negligible household income growth and the virtually guaranteed eventual increase in interest rates, should not the long-term outlook for single family value change be moderate at best? Fortunately, home ownership is not just an investment as it provides the benefit of allowing the buyer to live where they choose.

Commercial and industrial property values are also affected by rates for debt, while necessity and/or anticipated yields drive the market. So then, when the economic recovery occurs, commercial and industrial property values should benefit. Conversely, if inflation increases should not such investments provide a hedge? Conventional wisdom says yes and is thereby supportive of investment in real estate. Having been through a few real estate cycles, it is my opinion that market timing, which includes the combination of asset pricing and debt cost, currently supports real estate investment.

It has taken years of overspending to put this nation into its current economic situation. Long-term structural economic repairs are necessary along with the pain that accompanies them. Real property value declines have been well publicized, however, the future is where profits will be made and real estate investments, whether user-driven or purely investment driven, remain worthy of serious

current consideration.

In his inaugural address, President John F. Kennedy said, "I do not believe that any of us would exchange places with any other people or any other generation." I hope that we, as a nation, will address our financial problems and make the tough decisions that need to be made for the long term health of the nation so that this statement will remain valid for generations to come.

William LaChance, MAI, SRA, is the 2010 president of the Mass. chapter of the Appraisal Institute and partner at Petersen/LaChance Realty Advisors, Danvers, Mass.

New England Real Estate Journal - 17 Accord Park Drive #207, Norwell MA 02061 - (781) 878-4540